

REPORT OF THE AUDITOR-GENERAL TO THE FREE STATE PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE NALEDI LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the financial statements of the Naledi Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2012, the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMFA) and the Division of Revenue Act of South Africa, 2011 (Act No. 6 of 2011) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. My responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the General Notice issued in terms thereof and International Standards on Auditing. Because of the matters described in the Basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer of opinion

Property, plant and equipment

4. The municipality did not review the residual values of property, plant and equipment at year-end in accordance with SA Standards of GRAP, GRAP 17, *Property, plant and equipment*, and did not assess whether there is any indication that its property, plant and equipment may be impaired in accordance with GRAP 26, *Impairment of cash-generating assets*, for the current and prior financial year. I have not determined the correct net carrying amount of property, plant and equipment as it was impracticable to do so. In addition, I was also unable to obtain sufficient appropriate audit evidence to confirm the balance of property, plant and equipment disclosed as R273 209 054 (2011: R274 540 781) in note 6 to the financial statements. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for property, plant and equipment

Accumulated surplus

5. The municipality did disclose the detail of the restatements made for prior year errors as required by GRAP 1, *Presentation of Financial Statements* and GRAP 3, *Accounting policies, changes in accounting estimates and errors*. I was unable to obtain sufficient appropriate audit evidence to confirm the balance of accumulated surplus amounting to R270 202 580 (2011: R250 262 522) as disclosed in the statement of financial position and in the statement of changes in net assets due to supporting documentation that could not be

obtained for the movement in the balance in the comparative figures, as well as the limitation on other balances in the statement of financial position. The municipality's records and information available did not permit the application of alternative procedures. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for accumulated surplus.

Revenue

6. Accounting policy note 1.12.1 is not in accordance with GRAP 9, *Revenue from exchange transactions*, since revenue from the sale of prepaid meter credit is recognised at the point of sale and not only at the stage when the municipality no longer retains continuing managerial involvement to the degree usually associated with ownership or effective control over the goods sold. As a result, the sale of prepaid electricity revenue was incorrectly recognised as revenue, instead of deferred income as required by GRAP 9. Due to the volume of transactions involved I could not quantify the extent of this misstatement. In addition, I was unable to obtain sufficient appropriate audit evidence to confirm the amount of revenue disclosed as R95 638 940 (2011: R77 505 812) in the statement of financial performance due to an inadequate system of internal control to account for revenue, the management of the filing system not functioning effectively and services not calculated and charged on a monthly basis. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for revenue.
8. Furthermore, I was unable to obtain sufficient appropriate audit evidence for the restatement amounting to R914 879 in the corresponding figure of revenue as disclosed in note 28 to the financial statements. Due to a lack of supporting documentation I could not perform alternative procedures to confirm the amount.

Consumer debtors

9. The municipality made a provision of R49 104 482 (2011: R48 655 630) for the impairment of consumer debtors, however this impairment was not assessed at year-end, for the current and prior year, in accordance with the International Financial Reporting Standard (IFRS) 7, *Financial instruments: Disclosures*, International Accounting Standard (IAS) 32, *Financial instruments: Presentation*, and IAS 39, *Financial instruments: Recognition and measurement*. As the relevant information was not available, I was not able to calculate what the impairment charge against consumer debtors and impairment losses expense should have been if IAS 39 had been applied correctly. The impact of this on the value-added tax (VAT), debt impairment and accumulated surplus balance could also not be determined. In addition, I was unable to obtain sufficient appropriate audit evidence to confirm the balance of consumer debtors disclosed as R65 854 923 (2011: R49 863 792) in note 3 to the financial statements. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for consumer debtors.
10. The municipality did not measure consumer debtors at amortised cost in accordance with IAS 39 and did not disclose the age analysis by major revenue source and by customer classification in accordance with IFRS 7, IAS 32 and IAS 39 and did not differentiate between receivables from exchange and non-exchange receivables in accordance with GRAP 1. The municipality did not comply with these requirements in the current and prior year.

Expenditure

11. I was unable to obtain sufficient appropriate audit evidence to confirm the amount of expenditure disclosed as R55 247 772 (2011: R83 138 487) in the statement of financial performance due to an inadequate system to account for expenditure, the management of the filing system not functioning effectively and transactions being recorded when payment is made instead of being recorded when goods and services are received. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for expenditure.

Trade and other payables

12. I was unable to obtain sufficient appropriate audit evidence to confirm the balance of trade and other payables disclosed as R27 155 491 (2011: R35 716 095) in note 12 to the financial statements due to an inadequate system of internal control to account for trade and other payables and suspense accounts not cleared at year-end. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for trade and other payables.

13. In addition, I was unable to obtain sufficient appropriate audit evidence for the restatement amounting to R10 763 167 in the corresponding figure of trade and other payables as disclosed in note 28 to the financial statements. Due to a lack of supporting documentation I could not perform alternative procedures to confirm the amount.

Employee-related cost

14. I was unable to obtain sufficient appropriate audit evidence as to the accuracy, completeness and occurrence of employee-related cost disclosed as R21 582 151 (2011: R21 813 993) in the statement of financial performance and note 20 to the financial statements due to supporting documentation that could not be obtained for payments made. The municipality's records and information available did not permit the application of alternative procedures. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for employee-related cost.

Commitments

15. Sufficient appropriate audit evidence to confirm the balance of commitments disclosed as R13 014 306 (2011: R0) in note 32 to financial statements could not be obtained due to the lack of a proper contract management system for the identification and recognition of contracts, a complete contract register or any other documents to enable me to quantify the commitments. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for commitments.

Contingent liabilities

16. Sufficient appropriate audit evidence as to the completeness and valuation and allocation of contingent liabilities as disclosed in note 32 to the financial statements could not be obtained due to the lack of legal confirmations on pending claims. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for commitments. The municipality's records did not permit the application of reasonable alternative audit procedures and I was unable to confirm all the information and explanations I considered necessary to gain adequate audit evidence as to the completeness and

valuation and allocation of pending claims included in contingent liabilities of R9 078 459 (2011: R9 145 918), as disclosed in note 33 to the annual financial statements.

Cash and cash equivalents

17. I was unable to obtain sufficient appropriate audit evidence to confirm the balance of cash and cash equivalents disclosed as R6 408 306 (2011: R4 376 599) in the statement of financial position. I was unable to confirm these amounts disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to these amounts disclosed for cash and cash equivalents and bank overdraft.

18. In addition, I was unable to obtain sufficient appropriate audit evidence for the restatement amounting to R3 038 171 in the corresponding figure of cash and cash equivalents as disclosed in note 28 to the financial statements. Due to a lack of supporting documentation I could not perform alternative procedures to confirm the amount.

Unspent conditional grants and receipts

19. Sufficient appropriate audit evidence to confirm the balance of unspent conditional grants disclosed as R3 568 835 (2011: R2 291 794) in note 13 to the financial statements and the occurrence, accuracy, classification and completeness of revenue from grants and subsidies could not be obtained due to the lack of accurate reconciliations between the opening balance of unspent grants and the balance unspent at the end of the financial year. In addition, documentation to establish if all transactions took place according to the conditions of each grant and whether the expenditure against the grants should have been transferred to revenue in the statement of financial performance could not be supplied. I was unable to confirm these amounts disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the amounts disclosed for unspent conditional grants and receipts.

20. In addition, I was unable to obtain sufficient appropriate audit evidence for the restatement amounting to R15 019 321 in the corresponding figure of unspent conditional grants and receipts as disclosed in note 28 to the financial statements. Due to a lack of supporting documentation I could not perform alternative procedures to confirm the amount.

Other receivables

21. I was unable to obtain sufficient appropriate audit evidence to confirm the balance of VAT receivable of R2 972 625 (2011: R8 546 940) as disclosed in note 4 to the financial statements due to an inadequate system of internal control to account for VAT, general ledger accounts not used for VAT calculation purposes and reconciliations not performed. In addition, cases were identified where input VAT was not claimed on claimable expenditure and where input VAT was erroneously claimed. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for VAT receivable.

22. In addition, I was unable to obtain sufficient appropriate audit evidence for the restatement amounting to R7 352 967 in the corresponding figure of other receivables as disclosed in note 28 to the financial statements. Due to a lack of supporting documentation I could not perform alternative procedures to confirm the amount.

Investment property

23. The municipality did not disclose investment property in accordance with GRAP 16, *Investment property*. The municipality did not comply with these requirements in the current and prior year. In addition, I was unable to obtain sufficient audit evidence to confirm the balance of investment property disclosed as R2 520 000 (2011: R1 148 268) in note 7 to the financial statements due to an inadequate system of internal control to account for investment property and the management of the filing system not functioning effectively. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for investment property.

Fruitless and wasteful expenditure

24. I could not be provided with sufficient appropriate audit evidence that management has properly identified, investigated and recorded all fruitless and wasteful expenditure transactions during the current and prior year. Due to the limitations placed on the scope of the work performed relating to expenditure and the lack of a proper system of internal control to account for and identify fruitless and wasteful expenditure, there were no satisfactory alternative audit procedures that I could perform to confirm the completeness of fruitless and wasteful expenditure of R2 237 065 (2011: R2 383 553), as disclosed in note 29.1 to the financial statements.

Long-term liability

25. Sufficient appropriate audit evidence to confirm the balance of long-term liability of R537 281 (2011: R651 126) as disclosed in note 9 to the financial statements could not be obtained due to loan agreements, monthly statements or correspondence with finance provider and minutes of the meetings not provided. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for long-term liability.

Consumer deposits

26. I was unable to confirm that management has properly charged and accounted for all consumer deposits for the current and prior year. Consequently, I was unable to obtain sufficient appropriate audit evidence as to the completeness and valuation of consumer deposits of R400 622 (2011: R393 298), as disclosed in the statement of financial position, and the related disclosure in note 10 to the financial statements. The municipality's records and information available did not permit the application of alternative audit procedures regarding consumer deposits. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for consumer deposits.

Intangible assets

27. The municipality did not disclose intangible assets separately in the financial statements and also did not include an accounting policy for intangible assets in accordance with GRAP 102, *Intangible assets*, for the current and prior year. In addition, I was unable to obtain sufficient appropriate audit evidence to confirm the balance of intangible assets disclosed as R311 040 (2011: R311 040) in note 6 to the financial statements due to an inadequate system to account for intangible assets, software and computer programs. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the amount disclosed for intangible assets.

Irregular expenditure

28. I could not be provided with sufficient appropriate audit evidence that management has properly identified, investigated and recorded all irregular expenditure transactions during the current and prior year. Due to the limitations placed on my audit of expenditure and procurement management at the municipality and the lack of a proper system in place to account for and identify irregular expenditure, there were no satisfactory alternative audit procedures that I could perform to confirm the completeness of irregular expenditure of R108 442 (2011: R1 285 733), as disclosed in note 29.2 to the financial statements.

Employee benefits

29. IAS 19, *Employee benefits*, outlines the recognition and requirements pertaining to employee benefits. Contrary to these requirements, the municipality did not disclose post-retirement benefits and long service awards for the current and prior year. In the absence of appropriate records and information, I was unable to confirm the valuation and allocation and completeness of employee benefits for the current and prior year. Consequently, I was also not able to determine the effect on the other account balances and classes of transactions contained in the financial statements.

Provisions

30. GRAP 19, *Provisions, contingent liabilities and contingent assets*, requires that a provision should be made for the municipality's present obligation incurred as a consequence of its past use of landfill sites. Contrary to these requirements, a provision has not been made for the environmental rehabilitation costs of restoring the municipality's landfill sites for the current and prior year. In the absence of appropriate records and information, I was unable to confirm the valuation and allocation and completeness of provisions at year-end for the current and prior year. Consequently, I was also not able to determine the effect on the other account balances and classes of transactions contained in the financial statements.

Cash flow statement

31. I was unable to obtain sufficient appropriate audit evidence to determine whether the cash flow statement and the related notes were fairly stated for the current and prior year. Taking into account the misstatements and scope limitations identified in the financial statements, as set out in this report, I was unable to practically quantify the misstatements in the cash flow statement and notes thereto. Consequently, I was unable to determine the accuracy, completeness and correct disclosure of the cash flow statement and related notes.

Unauthorised expenditure

32. I could not be provided with sufficient appropriate audit evidence that management has properly identified, investigated and recorded all unauthorised expenditure transactions during the current and prior year. Due to the limitations placed on my audit of expenditure and procurement management at the municipality and the lack of a proper system in place to account for and identify unauthorised expenditure, there were no satisfactory alternative audit procedures that I could perform to confirm the completeness and valuation and allocation of unauthorised expenditure of R29 913 092 (2011: R39 279 523), as disclosed in note 29.3 to the financial statements.

Distribution losses and free services

33. Section 125(2)(d)(i) of the MFMA requires that the financial statements of a municipality must disclose particulars of any material losses. No distribution losses or free services provided were disclosed in the notes to the financial statements due to the municipality not implementing adequate control measures to reliably calculate these losses. In the absence of sufficient appropriate documents, I was unable to determine the total extent of the understatement in distribution losses.

Related parties

34. The municipality did not disclose the remuneration of key management personnel in accordance with the International Public Sector Accounting Standard (IPSAAS) 20, *Related-party disclosures*. The remuneration of key management personnel should be disclosed in total and for each of the following categories: short-term employee benefits; post-employment benefits; other long-term benefits; termination benefits and share-based payments. Contrary to these requirements, the municipality did not disclose the related-party transactions for the current and prior year that relates to the compensation of councillors and key management personnel.

Financial instruments

35. IFRS 7 requires the disclosure of information on liquidity risks, maturity analysis, sensitivity analysis and credit risk exposure relating to financial instruments. Contrary to the minimum disclosure requirements, the municipality's exposure to financial risks and how these risks were mitigated were not disclosed in the financial statements.

36. Furthermore, the municipality did not disclose gains or losses on financial instruments, trade receivables past due but not impaired, as well as the factors that the municipality considered in determining impairment as required by IFRS 7.

Additional disclosure in terms of MFMA

37. I was unable to obtain sufficient audit evidence to confirm the amounts disclosed in note 30 to the financial statements, due to differences between the disclosure and the supporting documentation that could not be explained. I was unable to confirm the amounts by alternative means.

Accounting policies

38. The municipality did not disclose the list of all GRAP standards issued, but not yet effective and the effective dates as required by GRAP 3. Furthermore, an accounting policy for judgements, sources of estimation uncertainty and key assumptions as required by GRAP 1 was not disclosed.

Financial sustainability

39. As a result of the matters described in the basis for disclaimer of opinion paragraphs, the municipality may be in a worse financial position than the position reflected in these financial statements. The difficulties being experienced by the municipality in recovering its consumer debtors, the potential negative effect of this tendency on the cash flows of the municipality and the inability to settle accounts payable within an acceptable period indicate that there is a risk that the municipality may be exposed to serious financial difficulties in terms of section 138 of the MFMA. The financial statements did not disclose any details of the uncertainty as per note 1.3 to the financial statements and have been prepared on a going concern basis. The municipality's accounting records did not provide sufficient appropriate audit evidence that the municipality is able to continue as a going concern.

Disclaimer of opinion

40. Because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

Emphasis of matters

41. I draw attention to the matters below. My opinion is not modified in respect of these matters:

Restatement of corresponding figures

42. As disclosed in note 28 to the financial statements, the corresponding figures for 30 June 2011 have been restated as a result of errors discovered during 30 June 2012 in the annual financial statements of the municipality at, and for the year ended, 30 June 2011.

Material impairments

43. As disclosed in note 3 to the financial statements, material losses to the amount of R448 852 (2011: R14 576 086) were incurred as a result of an increase in the provision for impairment relating to the recoverability of consumer debtors.

Material underspending of the conditional grant

44. As disclosed in note 12 to the financial statements, the municipality has materially underspent the budget on municipal infrastructure grant to the amount of R2 869 430. As a consequence, the municipality has not achieved its objectives of providing infrastructure for service delivery.

Additional matters

45. I draw attention to the matters below. My opinion is not modified in respect of these matters:

Material inconsistencies in other information included in the annual report

46. I have not obtained the other information included in the annual report and have not been able to identify any material inconsistencies with the annual financial statements.

Unaudited supplementary schedules

47. The supplementary information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

48. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages XX to XX of the annual report.

49. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury annual reporting principles and whether the reported performance is consistent with the planned development objectives. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the *National Treasury Framework for managing programme performance information* (FMPI).

The reliability of the information in respect of the selected development objectives is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).

50. The material findings are as follows:

Usefulness of information

Presentation

51. Improvement measures in the annual performance report for a total of 38% of the planned targets not achieved were not disclosed as required by section 46 of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 200) (MSA). This was due to inadequate internal policies and procedures over the processes pertaining to the reporting of performance information.

52. Section 46 of the MSA requires the disclosure of measures taken to improve performance in the annual performance report where planned targets were not achieved. Adequate and reliable corroborating evidence could not be provided for 62% measures taken to improve performance as disclosed in the annual performance report. The municipality's records did not permit the application of alternative audit procedures. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the validity, accuracy and completeness of the measures taken to improve performance.

Consistency

53. The MSA, section 41(c) requires that the integrated development plan (IDP) should form the basis for the annual report, therefore requiring the consistency of objectives, indicators and targets between planning and reporting documents. A total of 100% of the reported objectives, indicators and targets are not consistent with the objectives, indicators and targets as per the approved IDP. A total of 35% of the reported indicators are not consistent with the indicators as per the approved service delivery and budget implementation plan. A total of 52% of the reported targets are not consistent with the targets as per the approved service delivery and budget implementation plan. This is due to the lack of an adequate performance management system.

54. The MFMA, section 54(c) requires that the mayor must consider, and if necessary, make any revisions to the service delivery and budget implementation plan, provided that revisions to the service delivery targets and performance indicators in the plan may only be made with the approval of the council following approval of an adjustments budget. A total of 9% of objectives, 35% of indicators and 52% of targets reported in the annual performance report were inconsistent with the objectives, indicators and targets as per the approved service delivery and budget implementation plan. This was due to insufficient policies and procedures providing guidance on the requirements of the regulations.

Measurability

55. The FMPI requires that it must be possible to validate the processes and systems that produce the indicator. A total of 100% of the indicators relevant to the objectives were not verifiable in that valid processes and systems that produce the information on actual performance did not exist. This was due to the lack of an adequate performance management system.

Reliability of information

Reported performance not valid

56. The FMPI requires that processes and systems which produce the indicator should be verifiable. I was unable to obtain all the information and explanations I considered necessary to satisfy myself as to the validity of the actual reported performance relevant to 59% of the development objectives. This was due to the municipality's records not permitting the application of alternative audit procedures.

Reported performance not accurate

57. The FMPI requires that the indicator be accurate enough for its intended use and respond to changes in the level of performance. I was unable to obtain all the information and explanations I considered necessary to satisfy myself as to the accuracy of the actual reported performance relevant to 59% of the development objectives. This was due to the municipality's records not permitting the application of alternative audit procedures.

Reported performance not complete

58. The FMPI requires that documentation addressing the systems and processes for identifying, collecting, collating, verifying and storing information be properly maintained. I was unable to obtain all the information and explanations I considered necessary to satisfy myself as to the completeness of the actual reported performance relevant to 59% of the development objectives. This was due to the municipality's records not permitting the application of alternative audit procedures.

Additional matter

59. I draw attention to the following matter. This matter does not have an impact on the predetermined objectives audit findings reported above.

Achievement of planned targets

60. Of the total number of planned targets, only 28 were reached during the year under review. This represents 59% of total planned targets that were not reached during the year under review. This was as a result of the municipality not considering relevant systems and evidential requirements during the annual strategic planning process.

Compliance with laws and regulations

61. I performed procedures to obtain evidence that the entity has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the *General Notice* issued in terms of the PAA are as follows:

Strategic planning and performance management

62. The municipal council did not adopt an IDP, as required by section 25 of the MSA.

63. The municipality did not establish a performance management system that is in line with the priorities, objectives, indicators and targets contained in its IDP, did not clarify the roles and responsibilities of each role player in the functioning of the system, did not determine the frequency of reporting and the lines of accountability for performance, did not relate to the municipality's performance management processes and did not provide for procedures by which the system is linked to the municipality's integrated development planning processes, as required by section 38(a) of the MSA and MPPM Regulations 7(2)(c), (e), (f) and (g).

64. The municipality did not establish mechanisms to monitor and review its performance management system, as required by section 40 of the MSA.

65. The municipality did not:

- set appropriate key performance indicators as a yardstick for measuring performance, including outcomes and impact, with regard to the municipality's development priorities and objectives set out in its IDP
- monitor performance, with regard to each of those development priorities and objectives and against the key performance indicators and targets set
- measure and review performance at least once per year, with regard to each of those development priorities and objectives and against the key performance indicators and targets set
- take steps to improve performance with regard to those development priorities and objectives where performance targets are not met as required by section 41 of the MSA.

Budgets

66. Expenditure was incurred that was in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of sections 15 of the MFMMA.

67. Sufficient appropriate audit evidence could not be obtained that quarterly reports were submitted to the council on the implementation of the budget and financial state of affairs of the municipality within 30 days after the end of each quarter, as required by section 52(d) of the MFMMA.

Annual financial statements, performance and annual reports

68. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMMA. Material misstatements identified by the auditors in the submitted financial statements were not adequately corrected and the supporting records could not be provided subsequently, which resulted in the financial statements receiving a disclaimer audit opinion.

69. The annual report for the year under review does not include the accounting officer's assessment of the municipality's performance against measurable performance objectives

- for revenue collection from each revenue source and for each budget vote and the report of the audit committee, as required by section 121(3)(f) and (j) of the MFMA.
70. The annual performance report for the year under review does not include:
- a comparison with the previous financial year
 - measures taken to improve performance, as required by section 46(1) (b) and (c) of the MSA.

Audit committee

71. An audit committee was not in place, as required by section 166(1) of the MFMA.

Internal audit

72. An internal audit unit was not established, as required by section 165(1) of the MFMA as there was not a functional internal audit division at the municipality throughout the entire financial year. Consequently, the internal audit unit did not perform its duties required by section 165(2) of the MFMA, section 45(1) of the MSA and Municipal Planning and Performance Management Regulation 14(1).

Procurement and contract management

73. Goods and services with a transaction value below R200 000 were procured without obtaining the required price quotations as required by Supply Chain Management (SCM) Regulation 17(a) and (c).
74. Quotations were accepted from prospective providers who are not registered on the list of accredited prospective providers and do not meet the listing requirements prescribed by the SCM policy in contravention of SCM Regulations 16(b) and 17(b).
75. Sufficient appropriate audit evidence could not be obtained that goods and services of a transaction value above R200 000 were procured by means of inviting competitive bids and that deviations were approved by the accounting officer only if it was impractical to invite competitive bids, as required by the municipality's SCM policy.
76. Sufficient appropriate audit evidence could not be obtained that bid specifications for procurement of goods and services through competitive bids were drafted in an unbiased manner that allowed all potential suppliers to offer their goods or services, as per required by SCM Regulation 27(2)(a).
77. Sufficient appropriate audit evidence could not be obtained that bid specifications were drafted by bid specification committees which were composed of one or more officials of the municipality as required by SCM Regulation 27(3).
78. Sufficient appropriate audit evidence could not be obtained that invitations for competitive bidding were advertised for a required minimum period of days, as required by SCM Regulation 22(1) and 22(2).
79. Sufficient appropriate audit evidence could not be obtained that bids were evaluated by bid evaluation committees which were composed of officials from the departments requiring the goods or services and at least one SCM practitioner of the municipality as required by SCM Regulation 28(2).
80. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded to bidders based on points given for criteria that were stipulated in the original invitation for bidding and quotations, as required by SCM Regulations 21(b) and 28(1)(a) and Preferential Procurement Regulations.

81. Sufficient appropriate audit evidence could not be obtained that bid adjudication was always done by committees which were composed in accordance with SCM regulation 29(2).
82. Sufficient appropriate audit evidence could not be obtained that awards made to bidders, other than those recommended by the bid evaluation committee, were ratified by the accounting officer, as required by SCM Regulation 29(5)(b).
83. Sufficient appropriate audit evidence could not be obtained that the preference point system was applied in all procurement of goods and services above R30 000 as required by section 2(a) of the Preferential Procurement Policy Framework Act (PPPFA) and SCM Regulation 28(1)(a).
84. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded to suppliers based on preference points that were allocated and calculated in accordance with the requirements of the PPPFA and its regulations.
85. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded to bidders that scored the highest points in the evaluation process, as required by of section 2(1)(f) of the PPPFA.
86. Sufficient appropriate audit evidence could not be obtained that contracts were only extended or modified after tabling the reasons for the proposed amendment in the council of the municipality, as required by section 16(3) of the MFMA.
87. Sufficient appropriate audit evidence could not be obtained that all extension or modification to contracts were approved by a properly delegated official, as required by SCM Regulation 5.
88. Sufficient appropriate audit evidence could not be obtained that construction contracts were awarded to contractors that were registered with the Construction Industry Development Board (CIDB) and qualified for the contract in accordance with section 18(1) of the Construction Industry Development Board Act, 2000 (Act No. 38 of 2000) and CIDB Regulations 17 and 25(7A).
89. Construction projects were not always registered with the CIDB, as required by section 22 of the CIDB Act and CIDB Regulation 18.
90. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were only awarded to providers whose tax matters have been declared by the South African Revenue Service to be in order, as required by SCM Regulation 43.
91. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded only to bidders who submitted a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM Regulation 13(c).
92. Sufficient appropriate audit evidence could not be obtained that all contracts and quotations were awarded in accordance with the legislative requirements and a procurement process which is fair, equitable, transparent and competitive, as most of the bidding documentation could not be provided for audit purposes.

Human resource management

93. The competencies of chief financial officer and supply chain officers were not assessed promptly in order to identify and address gaps in competency levels as required by the Municipal Regulations on Minimum Competency Levels, regulation 13.
94. The municipality did not submit a report on compliance with prescribed competency levels to the National Treasury and the relevant provincial treasury as required by the Municipal Regulations on Minimum Competency Levels, regulation 14(2)(a).
95. The annual report of the municipality did not reflect information on compliance with prescribed minimum competencies as required by the Municipal Regulations on Minimum Competency Levels, regulation 14(2)(b).

Expenditure management

96. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred, accounted for creditors and accounted for payments made, as required by section 65(2)(b) of the MFMA.
97. The accounting officer did not take reasonable steps to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.
98. Money owing by the municipality was not always paid within 30 days of receiving an invoice or statement, as required by section 65(2)(e) of the MFMA.
99. An effective system of expenditure control, including procedures for the approval, authorisation, withdrawal and payment of funds, was not in place as required by section 65(2)(a) of the MFMA.
100. Unauthorised, irregular and fruitless and wasteful expenditure was investigated and as a result it was not recovered from the liable person, as required by section 32(2) of the MFMA.

Financial misconduct

101. Investigations were not instituted into all allegations of financial misconduct against officials of the municipality, as required by section 171(4)(a) of the MFMA due to the fact that unauthorised, irregular and fruitless and wasteful expenditure was incurred but was not investigated.

Conditional grants

102. The municipality did not comply with the requirements of the grant framework, as required by section 12(1) of the DoRA.
103. The municipality did not evaluate its performance in respect of programmes funded by the allocation and submit the evaluation to the transferring national officer within two months after the end of the financial year, as required by section 12(6) of the DoRA.
104. The municipality did not timely submit project registration forms, for projects it intended to implement in the financial year under review, to the provincial Department of Local Government, as required by the Division of Revenue Grant Framework, *Government Gazette No. 34280*.
105. Sufficient appropriate audit evidence could not be obtained that the allocations for the municipal systems improvement grant and the financial management grant were utilised

for purposes other than those stipulated in the grant framework in contravention of section 15(1) of the DoRA.

Revenue management

106. A tariff policy on the levying of fees for municipal services provided by the municipality was not adopted, as required by section 74(1) of the MSA and section 62(1)(f)(i) of the MFMA.

107. A credit control and debt collection policy was not implemented, as required by section 96(b) of the MSA and section 62(1)(f)(iii) of the MFMA.

108. A policy on the levying of rates on rateable property within the municipality was not adopted, as required by section 3(1) of the Municipal Property Rates Act, 2004 (Act No. 6 of 2004) and section 62(1)(f)(iii) of MFMA.

109. An adequate management, accounting and information system was not in place which recognised revenue when it was earned, accounted for debtors and accounted for receipts of revenue, as required by section 64(2)(e) of the MFMA.

110. Interest was not charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA.

111. Sufficient audit evidence could not be obtained that revenue had been reconciled on a weekly basis, as required by 64(2)(h) of the MFMA.

112. Accounts for municipal tax and charges for municipal services were not prepared on a monthly basis, as required by section 64(2)(c) of the MFMA.

Asset management

113. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.

114. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

115. Sufficient audit evidence could not be obtained that capital assets were permanently disposed with the approval of the council or the accounting officer, as required by section 14(2)(a) of the MFMA and Municipal Asset Transfer Regulation 5.

Liability management

116. A management, accounting and information system which adequately accounts for liabilities was not in place, as required by section 63(2)(a) of the MFMA.

117. An effective system of internal control for liabilities was not in place, as required by section 63(2)(c) of the MFMA.

Environmental

118. The municipality operated their waste disposal sites without a waste management licence or permit, in contravention of section 20(b) of the National Environmental Management Waste Act, 2008 (Act No. 59 of 2008) and section 20(1) of the Environmental Conservation Act, 1989 (Act No. 73 of 1989).

Internal control

119. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for disclaimer of opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

120. The accounting officer position was vacant for the year under review.
121. The acting accounting officers did not evaluate whether management had implemented effective internal controls by gaining an understanding of how senior management members had met their responsibilities in terms of preparing bank reconciliations, ensuring proper records management, maintaining an asset register and preparing the annual financial statements.
122. The acting accounting officers and senior managers did not take timely and adequate action to address weaknesses in the finance and supply chain management directorate, which resulted in non-compliance with applicable legislation and gave rise to unauthorised, fruitless and wasteful and irregular expenditure.
123. The acting accounting officers and senior managers of the municipality did not ensure that internal control procedures were developed, implemented and monitored to ensure that daily disciplines were performed and reviewed.
124. The lack of decisive action to mitigate emerging risks, implement timely corrective measures and address non-performance was evident by the failure of management to adequately address the external audit findings in a timely manner. The municipality failed to properly analyse the control weaknesses and implement appropriate follow-up actions that adequately addressed the root cause. This resulted in the audit findings in the prior year report being recurring in the current year.
125. The acting accounting officers and senior managers failed to implement adequate controls to ensure compliance with laws, regulations and internally designed policies and procedures. As a result, significant non-compliance issues were noted.

Financial and performance management

126. Effective performance systems, processes and procedures as well as the management thereof had not been adequately developed and implemented.
127. Inadequate filing procedures at the municipality resulted in limitations of scope during the current and previous year's audits. As a result significant difficulties were experienced in respect of the availability of information.
128. The financial statements were not properly reviewed for completeness and accuracy prior to submission for auditing. This resulted in many findings relating to incorrect disclosure.
129. The municipality did not have the capacity to address backlog issues and financial system problems, resulting in the need to appoint consultants. Consultants assisted with the preparation of an asset register and financial statements.
130. Finance staff had an insufficient understanding of the accounting framework. This contributed towards the numerous qualifications in the financial statements of the municipality.

Governance

131. The financial statements contained numerous inaccuracies, which are attributable to weaknesses in the design and implementation of internal control in respect of financial management and financial reporting, and weaknesses in the information systems.
132. The municipality did not have a documented fraud prevention plan. Internal control deficiencies were not identified and communicated in a timely manner to allow for corrective action to be taken. The implementation of external audit recommendations was not monitored. This resulted in the prior year audit findings not being substantially addressed.
133. Although the municipality had an internal audit division, it was not adequately resourced and functioning to identify internal control deficiencies and provide recommendations.
134. An audit committee and performance audit committee was not in place for the financial year.

Auditor-General
Bloemfontein
30 November 2012



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence